The Outlook: May 20, 2020

Strange new economic world . . . same old market, though.

We're living through the strangest economic event in the history of the world. As grim as it is, it's also really interesting to watch it unfold before our eyes, every day. In some ways (but not all, by any means) the rulebooks written from past economic experience have been thrown out, and we're discovering something new about how the global economy behaves in this strange world, also every day or so.

One of those strange discoveries, so far, has been the behavior of the oil market. Oil rose to the mid-$30's range today. It's safe to say that's been a surprise to almost every expert under the sun. They were all mighty impressed by the cliff-diving destruction of oil demand following the worldwide lockdowns—and they had a right to be impressed. It was extremely hard to imagine anything but $10 to $20 oil for a good while, as oil supply slowly fell, trying without success to catch up to oil demand (down there in the reefs at the bottom of the cliff already.)

But two surprising things, so far, have added up to the surprise in oil's price, itself.

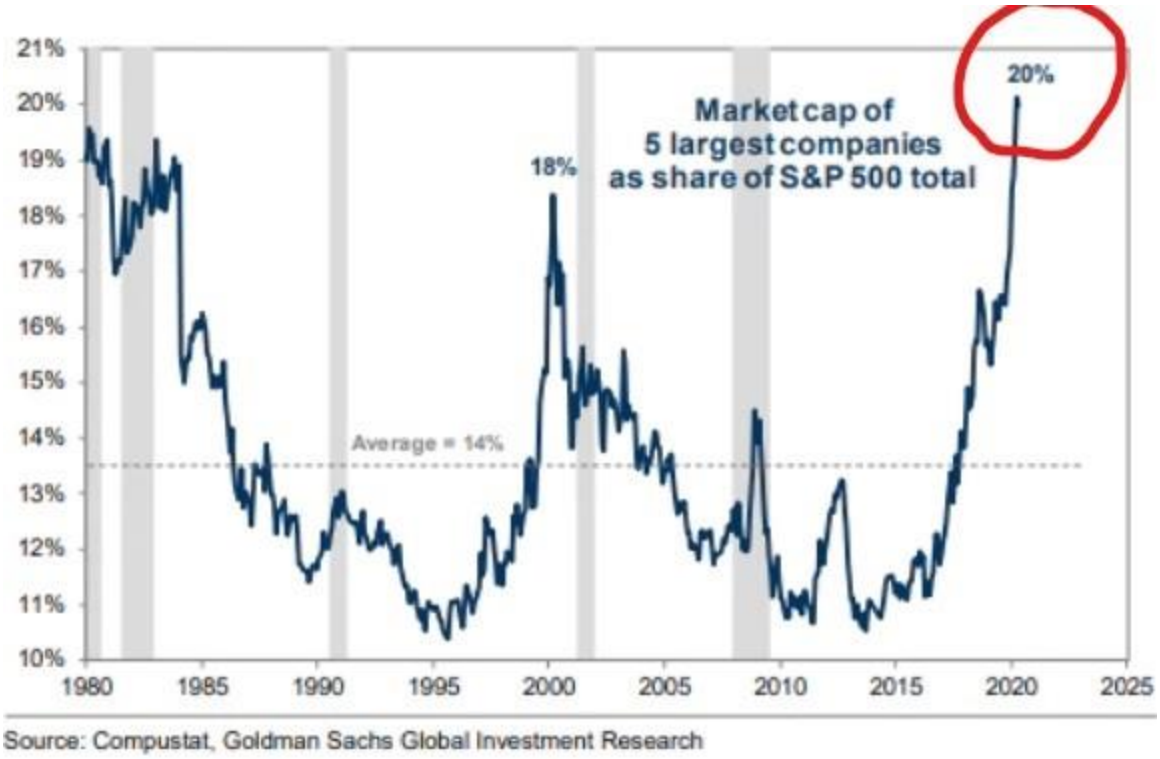
1. Oil supply is falling considerably faster than imaginable, a month ago. That "negative $40/barrel" headline, a few weeks ago, was clearly so terrifying to oil producers that they decided "gradually" just wouldn't do the job, when it came to cutting production.

2. Oil demand looks like it's rising faster than imaginable, a month ago. Lockdowns or not, all kinds of indicators show Americans getting in their cars and driving places, these past couple of weeks.

That brings us right to the Big Question, today: "Is the energy sector of the market a raving buy, or is it radioactive waste for too long to endure?" Let's look at 2 charts:

"Something isn't cheap until everyone else hates it. But it isn't really cheap until you hate it yourself." That green circle, showing that Energy's weighting in the market at 3.5% is the lowest in 30 years, may not prove oil is a raving buy . . . but it certainly captures a lot of hate, doesn't it?

Now let's look at the polar opposite end of things: market "love" reaching heights beyond the sun, the moon and the stars.



This picture gives us 40 years of history. At this moment, the 5 biggest of the Big Tech companies—Apple, Microsoft, Google, Amazon and Facebook—are valued at 20% of the entire value of the "large" U.S. stock market. That's the biggest and narrowest market "bet," so to speak, in the last 40 years of history.

That fact deserves to be contemplated for a while.

Why? The same pictures tell us why. Whether the market hates or loves something . . . it always changes its mind after taking it to extremes. It may be, of course, that these decades of history have run their course; that "things are different now"; that the Big Five Tech stocks will march from today's 20% to tomorrow's 30% of the whole pie, then move on to even more fantastic achievements . . . in sum, that the nature of the market itself has changed.

It would not be wise to believe that. It would be wiser to expect the market to stay true to its nature: meaning weakening performance of the Big Five, as a group, and strengthening performance of the Energy Sector, also as a group.

"It's a market of stocks, not a stock market," is yet another old saying with a lot of value. It means, "Let's pay attention to each operating business we own, and the valuation of its individual stock, rather than making judgments and action plans based on broad generalizations" . . . which is what the "stock market" actually is. That is why we own Microsoft, one of those highly-valued Five. And it's also why we own Conoco, Exxon, Shell and others—represented by those Energy Sector stocks down there among the reefs at cliff bottom. We own them because we understand their operating businesses, and the extreme doubts and anxiety riddling their stock valuations at the moment . . . and understanding both things tells us "Yes, they are in, or reasonably near, that "raving buy" neighborhood indicated by the green circle." As always, the surprising behavior of the price of oil recently does not tell us that Energy's rocket ride from

the bottom has begun. It certainly tells us, though, that when it does begin, this is how it will look . . . and that's all we really need to know.

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